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Mr. Chairman and Members of the Subcommittee:

We are pleased to be here to discuss the Internal Revenue Service's (IRS) progress in modernizing the computer systems that process tax returns. As you requested, we will discuss the challenges IRS is facing in planning its overall Tax System Modernization (TSM) program and describe the progress of two early modernization projects--the electronic filing and On-Line Entity (OLE) systems. We will also comment on the recent budget cuts IRS has sustained in the automated data processing (ADP) area.

TAX SYSTEM MODERNIZATION:  
IRS' CHALLENGE FOR THE 21ST CENTURY

IRS still processes tax returns using design concepts from the 1950s, such as batch processing and magnetic tape storage on reels. The system relies heavily on paper-driven, labor-intensive processes. As shown in the chart before you (CHART I) airplanes and trucks are used to move information across the country instead of modern telecommunications. As a result, data input and retrieval often take weeks, making service to taxpayers slow and sometimes unreliable.

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Tax System Modernization may well be the largest and most costly civilian modernization the government has ever undertaken. As shown in the chart now before you (CHART II) it is intended to move tax return information electronically to where and to whom it is needed. Since 1986, IRS has spent about \$120 million on its Tax System Modernization program, a major development effort that is estimated to cost several billion dollars and take the greater part of a decade to complete. As pointed out in our recent report<sup>1</sup>, this is IRS' third major modernization attempt since 1968. These earlier efforts were unsuccessful largely because of a lack of stable leadership, lack of accountability for them, and a lack of technical and managerial expertise.

Although considerable progress has been made with the current Tax System Modernization efforts, it is also beset with some uncertainty. As discussed in our report, IRS still needs to articulate what TSM is, how it will benefit the taxpayer, and the plans and schedule for making TSM a reality. Is it the beginning of a new way of doing business that would change dramatically how IRS services the taxpayer? Or, is TSM merely intended to lower the costs and

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<sup>1</sup>Tax System Modernization: IRS' Challenge for the 21st Century (GAO/IMTEC-90-13, Feb. 8, 1990).

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increase the efficiency of current operations? Either way, when does IRS plan to complete this modernization? This uncertainty is further illustrated by the continual changes in the number and scope of TSM projects identified in the budget from year to year which make it difficult to understand just what TSM is. Finally, the lack of a master plan makes it difficult to know whether and how the different systems will fit together into an integrated whole. For example, does TSM include a telecommunications network? If so, then why isn't such a network included among the budgeted projects?

To enhance the prospects of its success, IRS must first have a clear vision of its business goals in terms of improving service to the taxpayers and IRS' operations, and how TSM will meet these goals. Once a clear vision is established, IRS must marshall the best technical and managerial talent available to overcome the problems it continues to experience in developing major systems. The best talent must also be brought to bear on defining the technical platform--the hardware, software, and information--needed to achieve TSM's goals and make the major decisions impacting the design and development of the modernization. Key leadership and project management must be stable and competent so that the modernization can be carried out

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without the continued disruptions that IRS currently experiences.

Finally, the Congress must be provided with unambiguous information on the modernization. It is essential that IRS clearly lay out for the Congress the business goals of TSM, how the projects that comprise it will meet these goals, the priority of the projects, their estimated costs, and how and when the projects will be completed. Until IRS can do this, the focus of TSM will continue to be confusing.

I do want to emphasize that the Commissioner and his top managers have demonstrated a strong commitment to establishing the foundation to make modernization a reality in IRS. For example, IRS has recently reorganized its technology management structure to provide a single, top management focal point--the chief information officer--to oversee all IRS' technology programs. The Commissioner is also making a concerted effort to involve outside talent in the key modernization decisions.

We are hopeful that these efforts will help to clarify the uncertainties surrounding TSM, but they remain as of now. Until these uncertainties are resolved, it will be extremely difficult to assess the progress of TSM.

The Electronic Filing System illustrates the uncertainties surrounding TSM.

#### ELECTRONIC FILING

The Electronic Filing System evolved from an interim project that was first deployed in 1988 on a limited basis. This system has since been expanded and is now operational nationwide, even though fundamental planning is still being reviewed. As we testified last year, the system did not work as intended in either the 1988 or 1989 filing seasons.<sup>2</sup>

Although the system generally seems to be working well this year and over 3 million taxpayers have used the system as of March 15, 1990, we can't tell whether the system is a success because it is unclear how this system meets IRS' business goals for TSM and how it will be integrated into TSM. For example, is electronic filing ultimately intended to be used by all taxpayers or just those with personal computers? What share of the "taxpayer market" is IRS after

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<sup>2</sup>IRS' Progress in Implementing Its Electronic Filing and Communications Replacement Systems (GAO/T-IMTEC-89-2, Mar. 16, 1989).

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and by when does it hope to get it? It could cost the taxpayer \$15 or more just to transmit a return electronically. That amount could discourage some taxpayer participation. Is it intended to reduce costs for IRS? Until IRS defines the goals of the system as they relate to the overall goals of TSM, it is difficult for us to assess whether the progress of the Electronic Filing System is good or not.

#### On-Line Entity

The other project you asked about, the On-Line Entity system, also known as OLE, will allow IRS to validate a taxpayer's identity before sending tax return information to the master files in Martinsburg, West Virginia. However, because OLE is in the early stages of a pilot test, it has not had a major impact this year. Despite some minor problems, the system seems to be working and providing some benefit.

#### IRS' 1990 ADP BUDGET

Mr. Chairman, you also asked about the effect of any 1990 budget cuts on the modernization program. The 1990 IRS ADP budget sustained cuts of nearly \$100 million because of



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sequestration and increased salary costs. These cuts were most visible among projects aimed at increasing the number of computers and terminals available for responding to taxpayer inquiries and researching problem tax returns. Funds for projects that IRS designated as TSM were not cut in 1990.

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That concludes my statement, Mr. Chairman. I will be happy to respond to any questions you or other members of the Subcommittee may have.

# AO Existing Operations

